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Supreme Court, U.S.
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No. 801

Supreme Court of the United States

October Term, 1947.

WALTER G. HOUGLAND, JR., - - Petitioner,

versus

COMMISSIONER OF INTERNAL REVENUE, - - - - - - Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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Supreme Court of the United States

October Term, 1947.

No. _____.

WALTER G. HOUGLAND, JR., - - - *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, - *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

Your petitioner respectfully shows:

JURISDICTION.

The judgment of the Circuit Court of Appeals for the Sixth Circuit, a review of which is here sought, was entered on March 22, 1948 (R. 396).

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. A., Section 347(a)).

SUMMARY STATEMENT OF THE MATTER INVOLVED.

This case involves the question whether the partnership under the facts shown in the record and composed of petitioner, his wife and his mother was valid under the Federal income tax laws. The facts as found by the Tax Court are as follows (R. 375-380):

> "Walter G. Hougland, Jr. (hereinafter referred to as 'petitioner'), is the son of Walter G. Hougland and McGhee Hougland, the petitioner in Docket Nos. 4565 and 4998. Petitioner is a young man 29 years of age, residing and having his place of business at Owensboro, Kentucky. Petitioner's father, W. G. Hougland, died testate on November 7, 1939. The income tax returns of petitioner and of the estate of W. G. Hougland for the taxable period were filed with the collector of internal revenue for the district of Kentucky. When petitioner was about 15 years of age he began working for his father who, at the time of his death, had been engaged in the river transportation business for approximately 50 years. Petitioner and his wife, Dorothy Nell Hougland, were married June 15, 1933. To this union three children were born. Petitioner and his wife were divorced on or about January 20, 1944.
>
> "In the early part of 1937, petitioner unsuccessfully attempted to induce his father to buy an

additional towboat, whereupon he prevailed upon his father to assist him in acquiring such a boat. A contract was made with the Nashville Bridge Company for the construction of a towboat at a cost of approximately $158,000. The boat was named for his wife the 'Dorothy H.' Petitioner at the time had no resources of his own. His father loaned him $30,000 in cash to make the initial payment on the boat. Petitioner executed and delivered to his father three promissory notes in the amounts of $12,000, $10,000 and $8,000, respectively. Upon the completion of the boat, petitioner, with his father as a co-maker, executed notes for the balance of the cost. In April, 1938, the boat was put in commission, hauling gasoline for the Gulf Oil Company and the Gulf Refining Company, and has been exclusively in that employment ever since. The acquisition cost of the 'Dorothy H.' was paid off in full sometime in 1940 from earnings of the boat. Petitioner, upon starting operations, opened and carried on a bank account in the name of 'Towboat Dorothy H.', although the business was conducted under the name 'Hougland's'. Sometime the latter part of 1938 or the forepart of 1939, petitioner's father suggested to him that he would like petitioner's mother to have an interest in the boat and its business. On August 7, 1939, at petitioner's direction, his attorneys prepared a 'Bill of Sale' which was executed by petitioner purporting to transfer to his mother a one-half interest in the boat and its business at a price calculated to represent one-half of the cost of the boat less depreciation to the date of the sale. Both before and after the sale, petitioner's mother answered some telephone calls and telegrams since the business was operated from her home. The

mother had no funds of her own and it was understood that she was to execute her note for the purchase price, assume joint liability on the three notes aggregating $30,000, given by petitioner to his father, and two other notes in the respective amounts of $5,000 and $3,871.59, which were payable at the American National Bank of Nashville. It was also understood that the mother's obligation would be discharged out of her share of the earnings of the business. Thereupon petitioner's mother executed her note to him in the amount of $54,069.27, due one year from date with six per cent interest. At the time of the sale it was the understanding of the parties that petitioner was to manage the business, and that until the debts were paid there should be no salaries and that the drawings of the partners should be kept at a minimum. No written partnership agreement was entered into. From August 7, 1939, to the end of that calendar year petitioner and his mother each reported one-half of the net income of the business for tax purposes.

"Shortly after petitioner married, his wife, Dorothy, commenced work in his father's business as a bookkeeper. She had had no practical experience or training and her bookkeeping was of the crudest sort and not in accordance with good accounting practice. After petitioner started his operations with the towboat 'Dorothy H.', petitioner's wife also looked after his bookkeeping. For her services as bookkeeper she received a salary, the amount of which was divided between the two businesses.

"On January 1, 1940, petitioner and his mother executed a 'Bill of Sale' transferring to petition-

er's wife a one-third interest in 'Hougland's', and its assets, which at the time consisted of the 'Dorothy H.' and a small tender, at a price equivalent to one-third of the depreciated cost of that equipment. Dorothy had no funds of her own with which to pay the purchase price of such third interest, and it was understood that she should pay for the same out of her part of the earnings of the business. Dorothy thereupon executed to petitioner and his mother her note for $39,131.66, due one year after date with six per cent interest, representing one-third of that portion of the depreciated cost of the equipment which had been fully paid. She also assumed joint liability with petitioner and his mother for the notes representing that part of the cost of the equipment then unpaid. At the time this transaction occurred it was understood that no salaries would be paid; that personal drawings would be held to a minimum; and that petitioner would continue to manage the business. Prior to that time Dorothy prepared the checks which were signed by petitioner; but afterwards she was authorized to, and did, sign 90 per cent of the checks. Sometime in 1940 she ceased keeping books for 'Hougland's' and for the Estate of Walter G. Hougland. For the calendar year 1940, petitioner, his mother and his wife, Dorothy, each reported and paid income taxes on one-third the net income of 'Hougland's'.

"Sometime in 1940 a contract was made with the Nashville Bridge Company for the construction of another towboat to be known as the 'Walter G'. A substantial cash payment was made out of the earnings of 'Hougland's'. When this boat was completed, petitioner, his mother, and Doro-

thy executed their joint note to the Nashville Bridge Company for $125,000, payable in monthly installments of $5,000 each, and a note for $4,502.28, the aggregate of these two notes representing the unpaid part of the cost of the boat. These notes were paid off out of 'Hougland's' earnings by August 3, 1943. Up to that date, except for relatively small personal drawings, substantially all the net income of 'Hougland's' was applied to the payment of the notes executed for equipment, and to the payment of the income taxes of the three individuals. Neither petitioner's wife nor mother had income from 'Hougland's' to apply upon their individual notes executed by them for the acquisition of their respective interests. In 1939 and until they were divorced in 1944, petitioner and his wife resided in his mother's home and the household expenses were paid out of funds withdrawn from 'Hougland's' on the agreed basis of two-thirds for petitioner and one-third for his mother. The office of 'Hougland's' was at the home of petitioner.

"Petitioner's father died on November 7, 1939. Under his will, petitioner received 2/5ths, his mother 1/5th, and James Hougland, a son by the first marriage, 2/5ths of the entire estate, including his river craft and business. The river transportation business of the decedent was conducted by his estate until the estate was finally settled on October 3, 1940. Upon the final settlement of the estate, the business was conducted by a partnership under the name of 'Walter G. Hougland Sons' under the management of the petitioner. The partners were petitioner, his mother, and James Hougland, a son of Walter G. Hougland by a prior mar-

riage. Each had the same interest in that partnership as they had received under the will. James Hougland died in 1940 and his 2/5ths interest was divided between his widow and their two children, each taking a two-fifteenths interest in the partnership.

"On January 1, 1941, petitioner, with the consent of his other partners, transferred to his wife, Dorothy, one-half of his two-fifths interest in the partnership and assets of 'Walter G. Hougland Sons' for $42,325.25. Dorothy executed and delivered her demand note for $42,325.25, with the understanding that the note was to be paid off out of her interest in the earnings of the partnership. As of February 12, 1945, all of that note except $8,500 had been so paid. The bona fides of this latter partnership is not in issue.

"In 1943 marital dissension developed between petitioner and his wife, Dorothy, and they concluded to, and did, separate. An agreement in settlement of the wife's property rights was executed on December 15, 1943. The agreement contemplated a divorce, and the parties shortly thereafter were divorced and the custody of their three minor children was awarded to the wife. In the property settlement it was finally agreed that petitioner would pay the $150,000 demanded by Dorothy, with the proviso that Dorothy would make provision for the children by placing her interest in 'Hougland's' and 'Walter G. Hougland Sons' in trust for that purpose. Dorothy consented on condition that she be personally released from all obligations she had incurred in acquiring her interest in the two aforementioned businesses, and her liability transferred to the trust estate. Petitioner and his

mother, at the same time, executed and delivered to Dorothy separate instruments releasing her from all personal liability in respect of the obligations she had assumed in connection with the acquisition of such businesses. It was the purpose of both attorneys representing the respective parties, in preparing the trust instrument, to protect, as far as reasonably could be done, the interests of the three infant children. It was for this reason that the trust instrument provided that the interest in the businesses constituting the trust fund could not be sold without the consent of the petitioner, if living; that the reinvestment of the proceeds of any such sale must be with his approval, and that the income of the trust could not be borrowed against for the purpose of acquiring a residence for Dorothy and the children without his written consent. Dorothy was named as trustee of the trust and, on account of her youth and lack of business experience, the attorneys felt that the foregoing provisions would tend to safeguard the integrity of the trust funds. The trust instrument provided that in the event of the death of Dorothy, petitioner, if living should nominate her successor. This provision was not inserted in response to any claim of right on the part of petitioner, but because the attorneys considered that, as father of the children, he would be the proper person to name such successor. The trust was to terminate on the date the youngest of the three children became 21 years of age or, if he should die before reaching that age, then on the date the youngest living child should become that age. In the event all three children should die before reaching the age of 21, the trust was to terminate and the trust property was to vest in the petitioner, if living, or if dead, in his heirs.

"The partnership return filed under the name 'Hougland's' for the year 1940 disclosed a net income of $94,834.62, allocated equally among petitioner, his mother and his wife. These three individuals, in each of their separate income tax returns, reported the receipt of $31,611.54. Their returns disclosed income tax liabilities as follows: petitioner, $8,158.92; his mother, $8,096.58; and his wife, $6,872.15. These amounts were paid by 'Hougland's' during the year 1941, in four equal installments on or about the respective due dates and were charged to the accounts of those individuals. The respondent included all the income of 'Hougland's for the year 1940 in petitioner's taxable income, under section 22 (a) of the Internal Revenue Code, on the ground that 'Hougland's' was not a bona fide partnership for income tax purposes."

The above-quoted findings of fact were made upon the uncontradicted testimony and cover every fact proven by petitioner, except two. On these two, the proof also was uncontradicted. One was that the earnings of the partnership business were in large part due to the equipment in which Dorothy Nell Hougland and petitioner's mother each had a one-third interest, rather than to the personal efforts of petitioner (R. 184). The other was that the provision in the trust deed, referred to in the next to the last paragraph of the Court's finding, to the effect that in the event the three children should die without issue the trust property should pass to petitioner or to his heirs, was inserted in the trust instrument without the knowledge of petitioner and through no demand on his part that the

trust instrument should contain any such provision. Both petitioner and his counsel, Honorable Wilbur F. Miller, now Judge of the United States Circuit Court of Appeals for the District of Columbia, testified to that fact and their testimony was not contradicted (R. 196, 237).

On the above facts, the Tax Court of the United States sustained the action of the Commissioner of Internal Revenue, who determined that the wife and mother of petitioner were not bona-fide partners in "Hougland's", but that the business was, in fact, that of petitioner and that the entire net income thereof for the taxable year 1940 was includable in the taxable income of petitioner (R. 382). The United States Circuit Court of Appeals for the Sixth Circuit affirmed this decision of the Tax Court on the ground that the facts found by the Tax Court were based upon substantial evidence and brought the case within the ambit of *Commissioner* v. *Tower,* 327 U. S. 280 (R. 396).

QUESTIONS PRESENTED.

1. Was the Circuit Court of Appeals in error in its conception that the cases of *Commissioner* v. *Tower,* 327 U. S. 280, and *Lusthaus* v. *Commissioner,* 327 U. S. 293, mandatorily require the outlawing of all partnerships between a man and his wife, and between a man and his mother, where the woman involved makes no substantial contribution to the partnership in the way of services and where her capital contribution originates with the man?

2. Was the Circuit Court of Appeals in error in holding that the ruling of *Commissioner* v. *Tower,* 327 U. S. 280, was applicable to a partnership between a son and his mother?

3. Was the Circuit Court of Appeals in error in holding that the rule of *Commissioner* v. *Tower,* 327 U. S. 280, was applicable to the interest of Dorothy Nell Hougland which she acquired from her mother-in-law, McGhee Hougland, and not from the petitioner?

REASONS RELIED ON FOR ALLOWANCE OF WRIT.

1. The decision of the Circuit Court of Appeals to the effect that a partnership between a man, his wife and his mother, in which the wife and mother make no substantial contribution to the partnership in the way of services, and in which the property contributed by them was received from the man, must, as a matter of law, be disregarded for Federal income tax purposes, was based upon a misconception of the decision of this Court in *Commissioner* v. *Tower,* 327 U. S. 280, and resulted in a decision of a Federal question in a way probably in conflict with that case.

2. The decision of the Circuit Court of Appeals, holding that the ruling of *Commissioner* v. *Tower,* 327 U. S. 280, was applicable to a partnership between a son and his mother, rendered a decision on an important question of Federal law which has not been, but should be, settled by this Court.

3. The decision of the Circuit Court of Appeals, holding that the rule of *Commissioner* v. *Tower,* 327

U. S. 280, is applicable, even though the wife's interest was not received by her from her husband, rendered a decision in conflict with the decision of another Circuit Court of Appeals on the same matter (*Durwood* v. *Commissioner,* 159 Fed. 2d 400 (8th C. C. A.); and see, also, *Alexander* v. *Commissioner,* 6 T. C. 804, and *Shulak* v. *Commissioner,* 6 T. C. 1260).

PRAYER FOR WRIT.

WHEREFORE, your petitioner respectfully prays that a writ of certiorari issue out of and under the seal of this Honorable Court directed to the United States Circuit Court of Appeals for the Sixth Circuit, commanding said Court to certify and send to this Court for its review and determination a full and complete transcript of the record and all proceedings by the said Court had in this case, numbered and entitled on its docket, No. 10442, Walter G. Hougland, Jr., v. Commissioner of Internal Revenue, to the end that this cause may be reviewed and determined by this Court, and for such other and further relief as to this Court may seem proper.

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Petitioner,

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BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I.

OPINIONS OF COURTS BELOW.

The opinion of the Tax Court (R. 374) was a memorandum opinion and is not officially reported.

The Opinion of the United States Circuit Court of Appeals for the Sixth Circuit was rendered on March 22, 1948, and has not yet been reported (R. 396).

II.

JURISDICTION.

The jurisdictional statement at page 1 of the petition for writ of certiorari is adopted.

III.

STATEMENT OF THE CASE.

The summary Statement of the Matter Involved in the petition for writ of certiorari is hereby adopted.

IV.

SPECIFICATION OF ERRORS.

(1) The Circuit Court of Appeals was in error in its conception that the cases of *Commissioner* v. *Tower,* 327 U. S. 280 and *Lusthaus* v. *Commissioner,* 327 U. S. 293, mandatorily require the outlawing of all partnerships between a man and his wife, and between a man and his mother, where the woman involved makes no

substantial contribution to the partnership in the way of services and where her capital contribution originates with the man.

(2) The Circuit Court of Appeals erred in holding that the ruling of *Commissioner* v. *Tower,* 327 U. S. 280, was applicable to a partnership between a son and his mother.

(3) The Circuit Court of Appeals erred in holding that the rule of *Commissioner* v. *Tower,* 327 U. S. 280, was applicable to the interest of Dorothy Nell Hougland which she acquired from her mother-in-law, McGhee Hougland, and not from the petitioner.

V.

ARGUMENT.

(1) The Decision of the Circuit Court of Appeals, to the Effect That a Partnership Between a Man, His Wife and His Mother, in Which the Wife and Mother Make No Substantial Contribution to the Partnership in the Way of Services, and in Which the Property Contributed by Them Was Received From the Man, Must, as a Matter of Law, Be Disregarded For Federal Income Tax Purposes, Was Based Upon a Misconception of the Decision of This Court in Commissioner v. Tower, 327 U. S. 280, and Resulted in a Decision of a Federal Question in a Way Probably in Conflict With That Case.

Commissioner v. *Tower,* 327 U. S. 280, holds that, if a wife makes a substantial contribution to the earnings of the income of a partnership by the rendition of services or through capital not originating with her husband, which she puts in the business, then, as a

matter of law, there is a legal partnership for income tax purposes. It does not hold that, if the capital contributed by the wife originated with her husband, that fact of itself outlaws the partnership for income tax purposes. This Court merely stated that the Tax Court may take into consideration the fact that a wife renders no service to the partnership, or the fact that the capital contributed by her originated with her husband, or a combination of these facts in determining whether the partnership is real within the meaning of the revenue laws. The opinion in the Tower case was primarily rested upon the proposition that the facts found by the Tax Court were sufficient to support its findings that the wife was not a partner in the business.

The Tower case would not be authority for holding that, if a husband owns an income-producing office building, which he has managed, and irrevocably conveys by a deed a one-half interest therein to his wife, but the husband continues to manage the building, such part of the income from the building attributable to the wife's one-half interest should be taxed to the husband. Likewise, if a husband owned all of the stock of a corporation, which he has managed and controlled, and irrevocably transfers and assigns to his wife a portion of that stock, the Tower case would not be authority for holding that the dividends thereafter paid on the stock transferred to the wife should be taxed as income of the husband. Further, if a husband owned a towboat, which he had leased to others under a charter party and made an irrevocable transfer of a one-half interest in that boat to his wife, the income at-

tributable to that one-half interest would not be taxed to the husband. The only difference between this and the case presented by this petition is that, instead of the boat being leased to others, it was operated by the joint owners. The test is not where the property contributed by the partner came from, but whether or not the contributed property was in truth and fact unconditionally owned by the person purporting to contribute it. In this case there was no evidence that would even support an inference that the transfers from the petitioner were not absolute. So far as the wife is concerned, this is demonstrated beyond all reasonable doubt by the treatment of the partnership property when she divorced the petitioner. Also, the uncontradicted testimony established that the earnings of the partnership business were in large part due to the equipment in which petitioner's wife and mother each had a one-third interest, rather than to the personal efforts of petitioner (R. 148).

(2) The Decision of the Circuit Court of Appeals That the Ruling of Commissioner v. Tower, 327 U. S. 280, Was Applicable to a Partnership Between a Son and His Mother Rendered a Decision on an Important Question of Federal Law Which Has Not Been, But Should be, Settled by This Court.

Commissioner v. *Tower,* 327 U. S. 280, and *Lusthaus* v. *Commissioner,* 327 U. S. 293, dealt strictly with a husband and wife partnership. Aside from the general rule laid down in the Tower case for determining whether a partnership is valid or invalid for income

tax purposes, those cases have no application to the partnership created in August, 1939, between petitioner and his mother, McGhee Hougland, through the sale by petitioner to her of a one-half interest in the boat and its business. This Court has never held whether or not the mere fact that a parent contributed no substantial service to a partnership with a child and that the property contribution made by the parent to the partnership originated with the child outlaws such a partnership for income tax purposes. In *Singletary* v. *Commissioner*, 155 Fed. 2d 207 (C. C. A. 5), the partnership there involved was not condemned because the property contributed by the parents originated with the child; it was condemned because the Circuit Court of Appeals found that there was substantial evidence supporting the finding of the Tax Court that there was no good faith partnership.

(3) The Decision of the Circuit Court of Appeals, Holding That the Rule of Commissioner v. Tower, 327 U. S. 280, Is Applicable Even Though the Wife's Interest Was Not Received by Her From Her Husband, Rendered a Decision in Conflict With the Decision of Another Circuit Court of Appeals on the Same Matter.

Dorothy Nell Hougland did not acquire her one-third interest in the partnership entirely from petitioner. At the time she acquired her one-third interest, petitioner and his mother, McGhee Hougland, each owned a one-half interest. They jointly sold a one-third interest in the boat and its business to Dorothy Nell Hougland. In effect, each of them sold a one-sixth

interest to Dorothy Nell Hougland. If the Tower and Lusthaus cases go to the limit claimed by the Commissioner, that is, if those cases decide that, if the wife's interest originates with her husband, the partnership is not valid, those cases still have no application to that one-sixth interest which Dorothy Nell Hougland acquired from McGhee Hougland. That interest did not come from her husband. In *Durwood* v. *Commissioner*, 159 Fed. 2d 400 (C. C. A. 8), the Circuit Court of Appeals for the Eighth Circuit reversed the Tax Court and held that, where the great bulk of the shares of petitioner's wife, son and daughter did not come from petitioner, but from his brothers, the facts were not within the Tower case and that the income on those shares could not properly be taxed to the petitioner. To the same effect are *Alexander* v. *Commissioner*, 6 T. C. 804, and *Shulak* v. *Commissioner*, 6 T. C. 1260.

Respectfully submitted,

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Petitioner,

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In the Supreme Court of the United States

OCTOBER TERM, 1947

No. 801

WALTER G. HOUGLAND, JR., PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Circuit Court of Appeals (R. 396–398) is reported in 166 F. 2d 815. The memorandum findings of fact and opinion of the Tax Court of the United States (R. 374–384) are not reported.

JURISDICTION

The judgment of the Circuit Court of Appeals (R. 396) was entered on March 22, 1948. The petition for a writ of certiorari was filed on May 12, 1948. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the court below erred in affirming the decision of the Tax Court holding that all the income derived from a so-called partnership, composed of the petitioner, his mother, and his wife, was taxable to petitioner.

STATUTE AND REGULATIONS INVOLVED

These are set forth in the Appendix, *infra*, pp. 9–11.

STATEMENT

This case involves a deficiency in individual income tax asserted against the taxpayer, Walter G. Hougland, Jr., in the sum of $29,930.04 for the taxable year 1940. (R. 385.)

The facts pertaining to the issue herein, as found by the Tax Court (R. 375–380), and affirmed by the court below (R. 397), may be summarized as follows:

The taxpayer, with the financial assistance of his father by whom he was employed, purchased a towboat for $158,000, and, under the name "Hougland's," engaged profitably in river transportation. In August, 1939, about two years after his purchase of the towboat, the taxpayer sold a one-half interest therein to his mother. She delivered to him her promissory note in the face value of one-half of the cost of the towboat, less an agreed depreciation, and assumed joint liability with her son on three promissory notes, aggregating $30,000, which he had delivered to his

father to cover the cash borrowed. The liability of his mother to the taxpayer, however, was to be discharged out of her share of the profits of the business. (R. 397.)

On January 1, 1940, the taxpayer and his mother "sold" a one-third interest in "Hougland's" to the wife of the taxpayer under virtually the same arrangements which had been made at the time the taxpayer sold a half interest to his mother. Neither the mother nor the wife had funds of their own at the time of the respective transfers to them; nor was there any change in the management or control of the business by the taxpayer after these transfers were made. Neither the mother nor the wife contributed any vital services to the operation of the business. (R. 397.)

Upon the basis of the foregoing facts the Tax Court, affirming the Commissioner's determination (R. 19–27), held that the alleged family partnership was not controlling for federal income-tax purposes and that, therefore, the Commissioner properly included all the income therefrom in the taxpayer's gross income for the taxable year 1940 (R. 382–383). The Circuit Court of Appeals affirmed (R. 396–398).

ARGUMENT

This is another case involving the taxation, for federal income-tax purposes, of the income of a so-called family partnership. The case

was properly decided by the Tax Court and the court below. No question is presented which requires further review. The courts below properly applied the standards enunciated by this Court in *Commissioner* v. *Tower,* 327 U. S. 280, and *Lusthaus* v. *Commissioner,* 327 U. S. 293, and the decision below is in accord, as well, with innumerable decisions of the Circuit Courts of Appeals and the Tax Court.[1]

In the *Tower* and *Lusthaus* cases, *supra,* this Court held that family partnerships erected upon gifts or unreal assignments of business capital, though effective under state law, are without federal income-tax significance if the arrangement produces no substantial change in the creation of the business income but merely a reallocation of it within the donor's or assignor's family. Whether the claimed partnership, so tested, has reality presents a question of fact for the Tax

[1] Other decisions also in accord in which the taxpayers' petitions for writs of certiorari have been denied by this Court during the present term are *Fletcher* v. *Commissioner,* 164 F. 2d 182 (C. C. A. 2d), certiorari denied, March 15, 1948, No. 566, this term; *Eisenberg* v. *Commissioner,* 161 F. 2d 506 (C. C. A. 3d), certiorari denied, 322 U. S. 767; *Wilson* v. *Commissioner,* 161 F. 2d 556 (C. C. A. 4th), certiorari denied, 332 U. S. 769; *Scherf* v. *Commissioner,* 161 F. 2d 495 (C. C. A. 5th), certiorari denied, 332 U. S. 810; *Belcher* v. *Commissioner,* 162 F. 2d 974 (C. C. A. 5th), certiorari denied, 332 U. S. 824; pending on petition for a writ of certiorari is *Quon* v. *Commissioner,* 165 F. 2d 215 (C. C. A. 9th), No. 791, this term.

Court whose conclusion is final if supported by substantial evidence. Unless the donee or assignee "invests capital originating with her or substantially contributes to the control and management of the business, or otherwise performs vital additional services, or does all of these things" (*Commissioner* v. *Tower, supra,* p. 290), the Tax Court is justified in concluding that the donee or transferee is not a real partner for tax purposes.

These principles are applicable here. The taxpayer's mother acquired her interest in the partnership by purchase from the taxpayer, and the wife in turn likewise acquired her interest by the purchase of one-half thereof from each the taxpayer and his mother.[2] Each paid for her interest with notes payable from the profits of the business, just as the wife purchased from her taxpayer-husband one-half of her partnership interest with notes payable from the profits of the business in the *Lusthaus* case, and as the father and mother purchased their respective partnership interests from their taxpayer-son and his wife in *Singletary* v. *Commissioner,* 155

[2] *Durwood* v. *Commissioner*, 159 F. 2d 400 (C. C. A. 8th)—relied upon by the taxpayer (Br. 18) for the contention that his wife's acquisition of her one-sixth interest from his mother was a *bona fide* transfer—is not to the contrary. There the respective partnership interests of the taxpayer's son, wife and daughter did not come from the taxpayer but from others—his brothers—whereas here the interest of the taxpayer's mother and wife admittedly came from him.

F. 2d 207 (C. C. A. 5th).[3] The passage of mere titular ownership of portions of the taxpayer's business capital to his mother and wife shifted two-thirds of his partnership interest to them nominally and in harmony with legal form. This, however, did not change the economic realities—the taxpayer nevertheless continued, as before, to produce the respective shares of the business income ascribed to them, and in so far as they were concerned the partnership was "merely superficial, and did not result in changing the husband's [taxpayer's] economic interest in the business." *Lusthaus* v. *Commissioner, supra,* p. 297.

Further support for the conclusion of the court below is furnished by the fact that the mother's and the wife's admission into the partnership as partners is not shown to have served any business purpose. (R. 376–377.) *Commissioner* v. *Tower, supra,* p. 289. Moreover, the principles laid down in the *Tower* and *Lusthaus* cases are equally applicable to situations where members of the family other than the wife, such as the fathers, mothers, sons or daughters become partners. *Singletary* v. *Commissioner, supra; Wilson* v. *Commissioner,* 161 F. 2d 556 (C. C. A. 4th), certiorari denied, 332 U. S. 769; *DeKorse* v. *Commissioner,* 5 T. C.

[3] *Singletary* v. *Commissioner*, 155 F. 2d 207 (C. C. A. 5th), is an example of a ruling that even though a partnership already exists, it does not follow that those who contributed neither capital nor services became *bona fide* partners thereof.

94, affirmed *per curiam,* 158 F. 2d 801 (C. C. A. 6th); *Mauldin* v. *Commissioner,* 155 F. 2d 666 (C. C. A. 4th); *Hash* v. *Commissioner,* 152 F. 2d 722 (C. C. A. 4th), certiorari denied, 328 U. S. 838, rehearing denied, 328 U. S. 879.

As is plain from its opinion, the Tax Court properly addressed itself to the critical question of "who earned the [business] income," which, it stated (R. 382–383), is determined by ascertaining whether the parties really intended to carry on the business as partners. *Commissioner* v. *Tower, supra,* pp. 286–287. It found, upon the evidence, that neither the mother nor the wife was a real partner for tax purposes (R. 383); neither had any funds of her own at the time of the transfer to her to pay for her partnership interest other than from the prospective earnings of the business, or partnership income to apply to her individual notes for the acquisition of her interest (R. 376, 377–378, 383); neither contributed any vital or substantial services to the operation of the business, or capital originating with herself (R. 376, 383); the taxpayer admittedly continued to manage, operate, and control the business after such acquisitions just as he had before (R. 376, 377, 383); and that substantially all the partnership income was used to pay the liabilities incurred for the acquisition of the equipment of the partnership business (R. 375, 377–378, 383). Thus no new capital, services, control, or management was added.

CONCLUSION

The decision of the court below is correct. It turns upon and is supported by the facts, and presents no question calling for further review. There is no conflict of decisions. The petition should therefore be denied.

Respectfully submitted.

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MAY 1948.

APPENDIX

INTERNAL REVENUE CODE

SEC. 11. NORMAL TAX ON INDIVIDUALS.

There shall be levied, collected, and paid for each taxable year upon the net income of every individual a * * * tax * * *.

* * * * *

(26 U. S. C. 1940 ed., Sec. 11.)

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

(26 U. S. C. 1940 ed., Sec. 22.)

SEC. 181. PARTNERSHIP NOT TAXABLE.

Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity. (26 U. S. C. 1940 ed., Sec. 181.)

SEC. 182. TAX OF PARTNERS.

In computing the net income of each partner, he shall include, whether or not distribution is made to him—

* * * * *

(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183 (b). (26 U. S. C. 1940 ed., Sec. 182.)

SEC. 3797. DEFINITIONS.

(a) When used in this title, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof—

* * * * *

(2) *Partnership and Partner.*—The term "partnership" includes a syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this title, a trust or estate or a corporation; and the term "partner" includes a member in such a syndicate, group, pool, joint venture, or organization.

* * * * *

(26 U. S. C. 1940 ed., Sec. 3797.)

TREASURY REGULATIONS 103, PROMULGATED UNDER THE INTERNAL REVENUE CODE

SEC. 19.22 (a)–1. *What included in gross income.*—Gross income includes in general compensation for personal and professional services, business income, profits from sales of and dealings in property, interest, rent, dividends, and gains,

profits, and income derived from any source whatever, unless exempt from tax by law. (See sections 22 (b) and 116.) In general, income is the gain derived from capital, from labor, or from both combined * * *.

* * * * *

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